

Executive Summary

**Improving Market Access for Certified
Forest Products from Central America
and Mexico**

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Improving Market Access for Certified Forest Products from Central America

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1. Introduction

This executive summary outlines work accomplished on the “LAC/HFTE Timber Certification” assessment financed by AID and contracted to International Resources Group, Inc. (IRG) via the EPIQ IQC. For the purposes of clarity, the project is henceforth referred to as “Improving Market Access for Central American Certified Forest Products.” This summary outlines project goals, major findings and proposed solutions to obstacles that limit the international trade of certified wood products from Central America and Mexico.

In January 1995, only 21 forestry operations covering 4.1 million hectares had been certified in the world. By late 1998, more than 100 operations covering over 12.3 million hectares had been certified across the globe with close to 250,000 hectares of forest certified in Central America and Mexico.

An unfortunate reality is that despite a growing number of forestry projects and companies becoming certified by organizations accredited through the Forest Stewardship Council (FSC), many of the pioneers in this field have not yet successfully introduced their products into the marketplace. While FSC certification yields many non-market benefits (public recognition, improved forestry operations, political acceptance, etc.), the inability of Central American entrepreneurs to receive concrete market benefits (price premiums, access, new products, etc.) may diminish the positive impacts of this market-based incentive.

The original idea of the LAC/HFTE assessment was to organize Central American producers and manufacturers of certified forest products by establishing a “Seller’s Group” that could pull disparate producers and manufacturers together. The IRG team recognized that the Seller’s Group concept needed to be refined to meet the various needs of certified operations ranging from Mexico to Panama. IRG organized meetings in Washington, D.C. and San Jose, Costa Rica to gather input from tropical foresters, marketing experts, economists, business people, managers and donors on how to narrow the focus of the assessment to enable productive results.

2. Specific Objectives

The following project objectives were identified based on the needs and experiences of the aforementioned consulted parties:

- Identify opportunities and existing barriers for the commercial trade of certified wood products, based on field visits, interviews, and analysis of the current situation of certified wood producers and manufacturers in the region, as well as that of buyers from outside of the region.
- Identify concrete and feasible mechanisms to resolve the major trade obstacles and to take advantage of market opportunities.

- Present the preliminary results and solutions to an international audience comprised mainly of members of the private sector involved in the certified wood products industry to obtain a ground-truthing of the team's findings and allow for further refinement.
- Identify sources of financing to help "green businesses" dedicated to the trade of certified wood products.
- Serve as a linkage between producers and buyers to allow the sharing of experiences and facilitate entrance into the marketplace.

3. Area of Focus and Audience

The IRG Team focused its efforts on the following three forested regions of the Isthmus:

1. The Selva Maya (Belize, Guatemala, Mexico), a region full of both positive and negative experiences in the commercialization, production and marketing of certified products.
2. Nicaragua, which in spite of being a region with no certified operations yet, remains a country with a relatively high interest in the subject; this due in part to the large forest resource and the private sector's focus on international markets and capital.
3. Costa Rica due to its great diversity in examples including plantations, community projects, and large, vertically-integrated companies.

While Honduras was not given great attention due to limited resources and the unfortunate occurrence of Hurricane Mitch, limited information was gathered on this important area.

The specific target audience for the project was that niche of the private sector dedicated to working with certified wood, including producers, manufacturers, retailers, wholesalers and brokers both regionally and across the globe. The IRG team decided to actively seek out such individuals to build upon their valuable experience in the field.

4. Summary of Problems

Many of the problems of the forestry sector in the region are the result of structural deficiencies that are not due to, nor may be resolved through, forest certification. Furthermore, the problems found in the trade of certified products are identical to those found in the trade of uncertified products. The following summary of obstacles is organized by sector to facilitate understanding of the issues faced by each link in the Value Chain.

4.1 Producers

Technical Obstacles

- Small management areas with relatively low volumes of commercial species that make it difficult for producers to meet the international demand for large volumes.
- Dispersed producers do not sell wood as a group.
- Lack of adequate planning from the perspective of consistent volume, grade and species availability.

Market Obstacles

- Large demand for well-known primary species such as mahogany and spanish cedar, but extremely little demand or market recognition of lesser-known secondary species.
- Unrealistic demand for high quality (i.e. top grade) wood whereas much of the available wood from the region is of varied quality.
- Dispersed producers with little market knowledge are unable to evaluate fluctuating prices for a particular species.
- Lack of business experience or knowledge of international market requirements.
- General inability to produce products of acceptable quality to the international market such as:
- Variable grading that does not correspond to international standards.
 - Poor physical quality problems including problems with wood, pin-worms, blue stain, etc.
 - Wet, un-dried wood (the market generally requires kiln-drying down to 12% humidity).
 - Incorrect dimensions on cut lumber.
 - Low utilization efficiencies of available volumes.
 - Low quality packaging and marketing of final product.
 - Inconsistent production.
 - Inadequate storage that results in end-checking.
- Many artisan or community based forest enterprises projects have been unable to link their unique products to the appropriate niche market.

Financial Problems

- Lack of available capital at the time it is needed to finance logging operations or processing. Furthermore, available capital is offered at high interest rates, banks are reluctant to finance lesser-known economic activities such as forestry, or foreign transfers are complicated.
- Many producers maintain unrealistic expectations regarding the value of their products.
- There are few functioning models of certified forestry operations that are actually profitable.
- Particularly for community-based operations, the value chain is quite long and prone to many players that have the net result of lowering returns to the actual producer and increasing costs to the end user.
- Small producers have higher management and certification costs per area or volume than large producers.
- Few practical mechanisms exist to incorporate the intangible environmental services provided by certified forestry operations into the price received for the wood (i.e. clean water, biodiversity, tourism, etc.).

4.2 Manufacturers

Technical Problems

- Lack of a supply that corresponds with the real demand in terms of timeliness, product, quality, consistency, volume, etc.
- Lack of modern processing equipment that yields competitively priced products of sufficiently high quality to enter the international market.
- International markets require top grades and are not interested in lesser grades of wood.
- Lack of strategic planning and programming for long-term business development.

5. Proposed Solutions

As the array of problems is diverse, so are the solutions; there is no one solution for the whole region. Regardless, there is one common need to establish concrete actions that facilitate the efficient flow of quality products to new markets. While the IRG team identified several solutions, this summary limits its focus to technical, organizational, market, and financial issues

rather than those of a more political nature. While we recognize that policy and legal reforms are critical for sustainable forest management, the intent is that the following recommended actions are doable and could be financed through the private sector, international donor community or government collaboration. In essence, this represents the team's "to do" list. The effective implementation of these activities would go a long way to improving market access for certified forest products for Central America and Mexico.

5.1 Technical

Expand the area dedicated to forest management

While the designation of more forestry concessions would help increase wood supply, the current political trend is to move away of this traditional approach. Although community forestry concessions are increasing in Guatemala, there remains a regional need for clearly delineated and enforced private property, concession and/or protected area boundaries, as well as equitable land use zoning. These needs are strong in countries such as Nicaragua, Mexico and Guatemala. Addressing such issues should help stabilize productive areas for forest management. Much of this task would be linked to government and law enforcement agencies, but technical aspects would be most efficiently conducted through NGO's and internationally-funded projects.

Provide Practical and Relevant Training Opportunities

While substantial forestry-related training has been offered on inventories, silviculture, environmental impact analysis, and low-impact logging, there remains a distinct lack of management capacity in forest production. Training in areas such as harvest scheduling, mapping, calculation of annual allowable cut targets, operations planning, etc. is needed to ensure a consistent, efficient and cost-effective supply of wood.

Business-oriented training is also necessary in accounting and financial controls, inventory management, exportation, and strategic planning. Particularly relevant for community organizations is the need to improve in-house capacity for contract negotiations, administration, and organizational management (i.e. communications, decision-making, financial policies, etc.). Given the reoccurring problem of poor quality products, specific training on grading, drying, storage, wood treatments, sawmilling technology, packaging, and shipping is also requested.

One option for accessing technical trainers would be to work through the Small Business Association (SBA), retired executives, or for some topics, regional organizations such as INCAE or INCAP.

Central American Network for Producers and Manufacturers of Certified Wood

To date, most of the participants in the certified forestry industry are relatively inexperienced in the traditional wood products business. Although many of these firms and organizations may be practicing, certified forestry, maintain governmental or NGO support, and face a growing demand for their product, the majority really knows little about business. Each player has had varied successes and failures as they enter an unknown endeavor. Much would be learned by the sharing of experiences via a regional network. It would prove particularly relevant

to share experiences related to organizational models in the region, ranging from UNAFOC and the “Centro de Acopio” in Mexico, to community concessions in Guatemala, and joint ventures in Nicaragua.

To stimulate commerce, the network could also establish a web page to help share information related to product availability (specifically prices, species, grades, costs, etc.) with outside businesses with little knowledge of the region. While such a page would be somewhat costly and difficult to maintain, it could prove an effective tool to overcome language and cultural barriers.

In addition, the network could organize field-trips to successful sites, connect certified producers with the international marketplace and donor communities, and facilitate training. The network would also prove useful in lobbying for the interests of certified operations, not only on the political front, but also on the investment front (i.e. World Bank, BCIE, New Ventures, etc.) to help access the growing number of “green” investors. The network could be organized through local Forest Industry Associations (“Camaras Forestales”), perhaps as a sub-group of certified members.

Provision of Legal Assistance

Training in legal matters would not address the need for regular legal assistance on issues such as import/export regulations, contracts, buying and selling, foreign transactions, etc. Such aid is needed to help community operations from being taken advantage of by more astute businesspeople. As well, the legitimate purchasers of logs will prefer clearly-written contracts to inspire confidence that investments will not be lost, or that the first right of refusal on log purchases is respected. Sound legal assistance is to everyone’s benefit except the corrupt, and could be channeled through trade associations, or perhaps more appropriately, via organized producer groups as will be explained below.

5.2 Organizational

Formation of Producer Associations

Perhaps the over-riding theme that characterizes the Central American certified wood products industry (as well as the uncertified industry) is small and fractionated. Particularly from the perspective of the international market, the only way for certified producers to enter the international arena is by consolidating their volumes, thus giving them greater negotiating strength. A producer association or cooperative would be particularly fitting for certified operations in the Selva Maya and Honduras. Such groups could help organize harvests (to ensure that needed supplies are obtained and perhaps gain a price advantage in obtaining machinery or management services such as transportation, grading, drying, etc.), exercise quality control, market and sell wood, maintain a sort-yard (to be discussed), provide legal guidance, offer up-front “advances,” and facilitate communication between buyers and sellers.

Associations could also serve for group certifications such as the FUNDECOR model in Costa Rica or the COATHL model in Honduras. The group or Resource Manager model as

pioneered by SmartWood, allows for substantial cost savings and is a good way to get landowners working together, as well as possibly consolidating wood supply.

For such an association to function, clear rules related to decision-making, financial administration, profit-sharing, etc. must be established to avoid the kinds of problems faced by cooperative associations such as those found in Quintana Roo. The association must be able to withstand outside political pressures as well as internal strife. Despite the difficulty in managing an association, this would be a logical organizational first step. Associations generally protect the rights of their members, and could pave the way for other organizational developments such as joint-ventures. These are no small benefits since virtually all of the respondents spoke of being taken advantage of and needing some type of organization to protect their interests.

Establish Sort-yard to Gather and Store Wood for Sale

The aforementioned association (or other such model) could carry out the important function of gathering, sorting, grading, and storing logs or lumber from certified sources. Sort-yards allow buyers to purchase the exact species and grade that they want, and also help producers to sell the full range of their products. Such an approach can be more economically beneficial to the producer than the usual “camp” or “mill run.” Progress is currently underway to develop such a model in Guatemala.

Utilize Agents or Distributors to Access Specific Markets

Many individual operations have traditionally utilized an individual agent to market and distribute their products, and earn a percentage from total revenues generated. Another consideration would be for the agent to represent the aforementioned association of producers, or perhaps to purchase the wood out-rights for sale outside of the region. This approach would be simpler to initiate than other models, but its success depends on the ability of the agent to sell a product.

Establish Producer-Manufacturer Alliances

In Oregon, there has often been strong dis-connects between the log supply and the mill. However, the days when mills simply bought logs that were brought to their doors are ending. Increasingly, manufacturers are looking to establish stable and long-term relationships with those who supply their logs. In the case of the Impulsosores Suchitecos of Guatemala, the owners of logs are subcontracting a local mill for the processing. Generally, the producer carries out the management activities, whereas road building, extraction, transportation and milling are the responsibility of the manufacturer. While more traditional businesses may resist the idea of business alliances with “campesinos,” the progressive business survivors are jockeying for position to link up with producers.

It appears that producer-manufacturer alliances are “win/win” situations that result in the following benefits:

- lower fixed costs and lesser need for capital investment for the mill;
- improved community image for the mill;

- addition to a community's own wood source without needing to assume additional exposure or costs associated with the purchase of land;
- each member can concentrate on their areas of expertise: growing and selling trees, or growing and selling products.

Develop Joint-Ventures Between Producers and Manufacturers

A more advanced variation on the above alliance model is the joint-venture where an external company provides funds or other resources to the producer or mill to cover management, harvest, and manufacturing costs. Theoretically, all participants contribute resources of relatively equal value, be they logs, processing knowledge, access to markets, or capital, and all participants share risks. In short, this is a shared business where different forms of capital are brought to the table and result in economic benefits for all involved.

While this model may not seem that innovative, it is actually quite unusual, particularly when community forestry operations are involved. Most of the examples of joint-ventures involve plantations owned by small landowners. In such cases, the mill provides technical assistance and resources for establishing and maintaining the plantation with the contractual obligation to buy the resulting product at a certain price. Contingency clauses are necessary to cover both buyer and seller in the case of plantation failures or drastic market changes.

5.3 Market

Introduce Unique Products to Unique Markets

The U.S. market for figured, or otherwise unique wood, wood residues perceived to be of lesser-value, varied grades, or rustic, traditional products is small but growing, and currently not well tapped by C.A. producers or manufacturers. It was interesting to note that there is an interest in what, for lack of a better term, we call unique products. This is a high-end, discerning niche market that recognizes the unique nature of a product more so than the general wood commodity industry that is more oriented toward consistent volumes of the same product. Given the diverse nature of the regions forests and businesses, such markets would seem to be a particularly appropriate fit.

Direct contacts with architects, designers and artists are needed so that key players can become acquainted with the region, see and feel the story of the place, learn the characteristics of the species, and understand constraints. Trade organizations, industry associations and embassy programs could be utilized to organize targeted visits, round tables, or trade fairs with participants from organizations such as the American Society of Architects (ASA), the American Society of Internal Design (ASID), etc. The idea is to provide "Unique Products for Unique Markets" by utilizing creativity to meet small and specific orders, rather than simply trying to compete in the commodity business. Frankly put, the low prices and high volumes of tropical wood from countries such as Indonesia will make it difficult for Central American producers to compete on the international market (even given the region's geographic proximity to the U.S. market).

Develop Local Markets for Certified Products

Despite the interest and promise of export markets, one must not forget that the majority of the wood harvested in C.A. and Mexico is consumed in the region. As the area's environmental consciousness and willingness (or ability) to pay for environmental protection grows, it seems logical that interest in certified wood would also grow.

How to increase local demand? A good first step would be to focus educational efforts on high-end architects and developers with both national and international clients. General field trips that take prospective purchasers into the woods or put them in contact with suppliers have been conducted in the U.S. and are successful in developing interest in certification. Projects such as hotels, restaurants, embassies, international resorts or housing developments, etc. should all be targeted as potential users of certified wood. Another worthwhile effort would be to encourage the specification of certified wood in public works projects such as new buildings or school furniture for example.

Organization of Trade Round-Tables

As the skill and sophistication of certified producers and manufacturers increase, the use of trade meetings will become even more beneficial. The simple act of bringing together producers and buyers can yield powerful results (as shown in Bolivia). In fact, the final capstone event of the IRG project successfully linked businesses, several of which are functioning successfully today. In short, if an organization can prepare the meeting venue, business will result.

5.4 Economic

Establish and Distribute a Regular Price Bulletin

All members of the Value Chain would benefit from a periodic price report for logs and lumber on either a regional basis (i.e. the Selva Maya) or for all of Central America and Mexico. Such a report would help moderate price fluctuations by allowing all players to know the "going rate," negotiate a fair price, and promote the certified forest products industry as a legitimate business enterprise within the country's financial and political communities, as well as foment greater industry efficiencies. These bulletins could be modeled after the "Saw-Log Report" or "Random Lengths," both of which are representative of a common approach to facilitating wood products throughout the world.

For such a model to function, a neutral private party would be responsible for determining prices paid for logs and/or lumber of different grades and species. Institutions such as AGROEXPRONT in Guatemala and the Camara Forestal in Costa Rica could contribute to this task. Such reports would come out quarterly perhaps, and could also include unbiased and accurate market information.

Creation of a Certified Forestry Fund

Many producers are forced into unfavorable business arrangements because their sources of capital to fund harvest activities are limited; they often obtain operating capital from whoever is available at the time they have a need, regardless of the terms. The creation of a loan mechanism to “float” harvest costs would give producers greater flexibility and allow them to “shop around” for the buyer that presents the most favorable offer. Such loans must be convenient and timely, and would generally need to be provided during the months of December to May when harvest operations are underway.

This funding mechanism could be established with governmental bodies only for certified operations, much like “fondos ecologicos” (such as established in Guatemala’s “Banco Rural”). These would provide favorable terms (low interest rates, long pay-back periods, uncomplicated procedures) to this specific target group in recognition of the societal benefits provided by certified forestry.

One option might be to establish a rotating fund on a country or region-specific basis whereby members of a cooperative or trade association compete among one another. The international donor community could provide starting seed capital. Evaluation and selection criteria as well as loan pay-back terms would need to be clearly spelled out. Group pressure would also help ensure that loans are paid back (similar to many successful rural banking programs that supply funds to low income groups). The selection committee would be comprised of different sectors (forestry, processing, finance, NGO, government, etc.) from different regions to ensure a balanced consideration of loan applications. Selection criteria would be diverse.

It would be useful to explore the FUNDECOR model in Costa Rica to develop a fund based on the development of a market for externalities, such as carbon sequestration, that are usually not recognized.